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FAILURES AND POSSIBILITIES IN RAILROAD REGULATION

BY T. W. VAN METRE

When in 1906 and 1910 the federal law for the regulation of railway transportation was amended to give the Interstate Commerce Commission the authority (1) to require railroad companies to make just and reasonable charges for their services, (2) to put a stop to objectionable discriminations, and (3) to forestall any attempts which the carriers might make arbitrarily to increase rates, it was hoped, and in many quarters believed, that the troublesome question of public regulation of rates on interstate traffic was definitely settled. During the period that witnessed the movement culminating in the improved federal legislation the state legislatures were active in dealing with the railroads, and virtually every state was given a commission clothed with authority to regulate rates on intrastate traffic. The "railroad problem" was regarded as solved. Private ownership and management were retained; an administrative organization designed to afford the public protection against exorbitantly high and unnecessarily discriminatory rates was established. It was thought that a policy which combined the double advantage of efficient private operation and effective public control would surely result in the development of a thoroughly satisfactory transportation service at rates reasonable to those who used the service and adequate for those who produced it.

Though this policy has been in effect more than a decade it does not seem to have had the entirely beneficial effect so generally expected. Expressions of dissatisfaction with the conditions of railway transportation have for some years grown steadily in number and in emphasis. While the complaints have not been due to the same causes which elicited protests and demands in former times, they have been none the less clamorous and insistent, and they have been concerned with matters just as vital to the general public, and with questions which touch an even greater range of interest than was previously involved. Owners and managers of railroad prop-

erty point to increased investment and declining returns, to bankruptcies and receiverships, to their inability to acquire investment funds necessary to enable the transportation system to keep pace in development with other branches of industry. The shipping public is resentful of continued car shortage, embargoes and impaired service, due to lack of equipment or to want of efficient railway organization, or to both. Railway labor, pressed nearer the subsistence level of income, asks for higher wages to meet the advancing cost of living, only to have the demand refused by employers, who, unable to increase arbitrarily the price of the commodity which they produce and sell, are themselves victims of increasing costs of raw materials and supplies, the prices of which are regulated neither by statute nor by commission. And in the midst of the gravest crisis in the history of the nation and of the modern world, we are confronted with the facts that the railway system of the United States is unable to meet the needs of the country; that while the system is probably more efficient than the railroad system of any other country, it has fallen far short of realizing the highest standards of economy and efficiency; that while the railways are handling a greater traffic than at any previous time they are falling short of supplying the demand for transportation; and that they are not even hauling the quantity of freight which they would possibly haul with their present equipment but with a different operating organization. In order that the people may secure food and fuel adequate to sustain life, in order to provide industry with raw materials, to save the tottering credit of the railroad companies, to anticipate the ominous situation which new demands on the part of railroad labor were about to create, and to make it possible for the country to take the effective part in the war for civilization which its huge resources and the will of its people warrant, the government has been compelled to take over the operation of the railroads. We have been forced to confess that our railroad policy has fallen far short of the ideal; the first acute emergency has compelled us to discard the entire structure of private operation and public control so laboriously and hopefully devised, of which so much was expected; by executive mandate the President is endeavoring to achieve the operating economies, long easily attainable but just as long wilfully neglected under the past policy of private management and public regulation.

The railroad problem is far from being "solved." It has entered a new, and, in most respects, a much more difficult phase. Why, after the long and apparently successful struggle to correct the wrongs of former days, are we compelled to acknowledge failure? Why are we confronted with questions more difficult and complicated than any previously encountered? And what is to be done in the future?

In answer it must be said that there are clear and definite grounds for complaint against both the system of private operation and the system of public regulation as they have hitherto existed. The outstanding fact about the system of private management is that it is inefficient because it has failed to achieve operating unity; it was for the purpose of securing a unification of the railroad line that the government assumed control of railroad operation. There is a general impression that the laws of the country have prevented unity of operation among the carriers, and a consistent attempt has been made to lay at the door of the government the failure of the carriers to coöperate in the use of their physical equipment. This impression is based on false assumptions. There is no federal law, and very few state laws, which stand in the way of coöperation among the carriers in the use of their facilities; the common use of cars, passenger terminals and tracks, is practised extensively, and it involves no violation of the law. The railroads have failed to "get together" merely because, in everything except the fixing of rates, the railroad business is a highly competitive business. The unification of terminal facilities and tracks requires that some carriers surrender certain monopoly advantages of location which they have long possessed, and such a surrender no company has ever been willing to make. There is hardly a large city in the country which has not provided a battleground for railroad strategists intent upon seizing and perpetuating the exclusive control of a favorable location. Railroad companies have captured and held with tenacious grasp the waterfront of our chief seaports and, assuming a dog-in-the-manger attitude, they have often failed to develop the property themselves and have forbidden the encroachment of others. Bodies of railroad workmen have fought pitched battles over choice bits of territory; millions of dollars have been expended in the defeat of aggressive competitors; public service has been a secondary consideration to monopoly privilege. The inefficient

and wasteful terminal systems in such great cities as New York, Philadelphia and Chicago have been enduring and impressive monuments to the lack of railroad unity. Sufficient money was wasted in the combat waged by the Wabash Railroad to enter Pittsburgh to construct a great unified terminal at that choked gateway from which it was necessary recently to divert all shipments of through freight.

It is useless to assume that the repeal of the anti-pooling clause of the Act to Regulate Commerce and the modification of the Sherman Law would pave the way for voluntary railroad unity. Those laws have not stood in the way of the operating unity sorely needed at many terminals, and the mere repeal of those laws will not affect the situation. Persons who place dependence in such legislative changes forget that former railway pools were organized solely for the purpose of controlling rates; pools were never intended to facilitate operating unity, and they never had such an effect. Railroad managers now accomplish, through informal rate agreements, all that they ever sought to accomplish through pools and formal rate agreements, and they are consequently entirely indifferent to the proposed changes in the law. Indeed the more astute managers are averse to these particular changes, which, if made, might create expectations on the part of the public which they have no inclination voluntarily to fulfill. There is no doubt that the formation of pooling agreements would make it easier for the railroad companies to effect the financial arrangements necessary to a plan of unified operation under private ownership, and if private operation is to be resumed it is desirable that pooling should be permitted; but the mere toleration of pools and rate agreements will not lead to the voluntary unification of physical facilities so long as railroad managers desire to continue their hold on their particular monopoly advantages.

In recognizing the fact that railroad managers have not gone as far as they might have done in improving the railroad service through unified operation we must bear in mind that scant measure of blame can attach to them for their failure. We do not expect a business man meekly to share his strategic advantages with every struggling rival. The ideal of American business has been competition, and the existing railroad laws are based upon the theory that railroads should be forced to compete with one another. Far

from compelling coöperative action among the carriers in the use of physical equipment, or for any other purpose, the law makers of the country have held steadfastly to the ideal of competition, endeavoring even to prevent railway coöperation in rate-making, a form of coöperation which is virtually indispensable to the satisfactory conduct of the railroad business. In pursuing this theory our legislatures have burdened our statute books with laws, designed ostensibly for the protection of the public, which have been probably a greater obstruction to the development of adequate railway service than the unfortunate policy of selfishness pursued by the railroad managers. Public regulation has scored as many errors, both of omission and commission, as has private operation.

The dual system of railroad regulation by state and federal authority is without doubt cumbersome and wasteful, and it has been a prolific source of conflict and misunderstanding. The state railroad and utilities commissions are not a conspicuous success from the standpoint of personnel. They are composed chiefly of lawyers whose main interests lie, if not in politics, in legal rather than in economic problems. Commissions of several states have been used as tools for disreputable political tactics; that they exist for the purpose of safeguarding one of the most vital business interests of the country seems to have eluded the understanding of not a few appointing officials. Ill-considered and unwise laws for railroad regulation have been passed with too great frequency; and the powers vested in commissions have often been used with injurious effects to the carriers, or just as often have remained unused to the detriment of the general public.

Underlying the entire bill of particulars against the present system of regulation, of which these counts are probably the most important, is the fact that virtually all legislation enacted for the purpose of controlling the practices of the railroad corporations is one-sided in character; it evidences a commendable effort to protect the shipping and travelling public from unfair treatment by the carriers, but it shows little evidence that the legislatures thought it would ever be necessary that special precautions be taken to safeguard the interests of the railroads. This situation, unfortunate though it be, is the quite natural result of the offensive attitude formerly assumed by the railroad interests. It was once a well-nigh universal custom of railroad officials to justify or to condone the

flagrant abuses of the transportation service, and it was their habit strenuously to combat all attempts made by legislative bodies to render their objectionable practices impossible. Total disregard by the carriers of the interests of the public which they served bred legislation in which little effort was made to consider the welfare of the railroads. Laws were of necessity fashioned as cudgels with which refractory selfish interests could be driven to a consideration of the rights of others and to a realization of their own duties and responsibilities; the stubborn opposition which the railroad interests exhibited to all legislation was chiefly responsible for the retaliatory character which the law assumed. The Act to Regulate Commerce, as amended, provides easy methods for the reduction of rates, and supplies only obstacles to the increase of rates; the Interstate Commerce Commission was definitely intended to be primarily a rate-reducing organization.

The necessity of using punitive methods in the past renders difficult the problem of forming a constructive program for the future. The old feeling of bitter resentment against the railway official of the "public be damned" type has not been eradicated. The average shipper looks with more complacency on rates which provide no net revenue for the carriers than upon rates which are ruinous to his own business. He has just as much difficulty in seeing that a reasonable rate involves the consideration of the welfare of the railroads as the railroad managers once had in seeing that reasonable rates involved a consideration of the welfare of the public. The old policy of brutal exploitation is having its natural, if undesirable, results.

A conspicuous effect of the new order has been the confession of former faults on the part of railway officials, a profession of repentance and a bid for forgiveness. All public regulation was once anathema; today regulation—"of the proper kind"—is accepted with apparent welcome. The almost universal spirit of willingness to receive guidance by public authority and the unanimous desire to let bygones be bygones speak well at least for the influence of past legislation with respect to moral regeneration.

It is an unfortunate thing that to many ears the professions of willing acquiescence in a new dispensation should smack strongly of deathbed repentance. "When the devil was sick" While it is unquestionably true that the majority of railroad officials

have seen a light, certain facts indicate in some quarters a want of sincerity, a lack of frankness, which, coupled with occasional regrettable lapses of conduct, tend to keep alive the old distrust and suspicions and to weaken belief in protestations of reform.

It would be easier to forgive and forget the excesses of railway capitalization indulged in a generation ago if, in the absence of proper administrative regulation, all railway officials would refrain from giving demonstrations of a present aptitude for similar excesses. The examples within the past few years of wanton wrecking of sound railroad financial structures for the purpose of enriching small groups of unscrupulous speculators have placed upon the record ample evidence that some of the trustees in charge of the transportation service are unfaithful to their trust and unfit to have a voice in the direction of public service. It is true that reputable railroad managers have condemned the acts of the speculators; but it is not customary for the public at large to discriminate carefully between the good and bad elements of any particular class.

Moreover virtually all railroad managers have endeavored to reap some advantage from the effects of the financial wrecking. A common feature of the widely published appeals for increased rates has been to call attention to the unprecedented mileage of railroad in the hands of receivers. It was widely advertised in 1915 that there was a greater mileage of line under the control of receivers than at any previous time in the history of the country, and this fact was earnestly presented as good evidence of the need for increased rates. A very brief analysis showed that two-thirds of the line in the hands of receivers had reached bankruptcy because of the shameful financial operations of the speculators who had secured control of the companies; the excessive mileage of insolvent railroad presented a much stronger argument for regulation of capitalization than for upward revision of freight rates.

Lapses of conduct have not been confined to buccaneering tactics in finance. The annual reports of the Interstate Commerce Commission record indictments and prosecutions for offenses which show every indication of having been wilful and deliberate infractions of the law. The persistence of attempts to evade or to violate the provisions of present laws serves to discourage disinterested individuals who otherwise would desire to help the cause of the railroads. Other acts have a similar effect. Just as one begins

to feel that the railroads are an object of persecution when a threatened strike brings about the enactment of a wage law, one's sympathy is subdued by the lack of candor shown by the railroad officials in waiting until the day after election to begin a test of the law in the courts.

Fallacious arguments and statements containing half truths weaken rather than help the position of the carriers. A statement widely circulated last year (1917) called attention to the fact that from 1907 to 1915 about five billion dollars was added to the capital account of the railroads, and that net income was thirty-three million dollars less in the latter year than in the former. From which it was deduced that the five billion dollar investment yielded a return that was thirty-three million dollars less than nothing, it being the apparent design to create the impression that because of the niggardly policy of the government this huge investment was in immediate danger of becoming a total loss. No mention was made of the fact that the year 1907 was an exceptionally prosperous year for the carriers, freight traffic being greater even than in the two succeeding years, nor of the fact that railway business in 1915 was at a relatively low ebb, traffic having been considerably less than in either of the two preceding years. Nor was it told that with the great increase of traffic in 1916 the rate of return on investment in Class I railroads (those having annual operating revenues in excess of \$1,000,000) was the greatest ever recorded. It might have been explained, too, that a large part of this investment, contributed chiefly from earnings, went to absorb the "water" of former years, which was always made to appear like real money in the investment accounts published before 1907. It is true that railroad income has showed a tendency to decline in recent years, but unqualified statements of this kind misrepresent the real conditions. They do more to frighten investors than does an adverse decision on an application for rate increases. In fact statements of this nature have aroused the suspicion that the carriers, by deliberately misrepresenting their condition, have endeavored to depress their own financial credit in order that their palpable inability to borrow needed funds on reasonable terms would bring an increase of rates which would enable them to pay for improvements out of earnings. Groundless as such a suspicion certainly is, its existence shows how it is possible for the railroads to arouse public

opposition by the very means they employ to win public sympathy and support.

It is highly desirable if private operation of railways is to be resumed that the retaliatory character of present railroad laws be eliminated, but such a desire will be difficult of attainment unless railroad authorities definitely abandon all lines of conduct which tend to keep alive the retaliatory spirit of the public. Misrepresentation of facts, violations of the law, and stock-jobbing must be halted if the confidence of the people is to be earned, and the desire to receive equitable treatment must be matched with evidence of willingness to act fairly. To the credit of railroad officialdom it must be said that a majority is evincing a spirit which promises well for the future. Unqualified abuse of present regulation is giving way to thoughtful discussions of its advantages and disadvantages; federal regulation of the issue of securities is advocated here and there; an honest endeavor is being made to suggest modifications in the present system of regulation which will provide for conserving the interests of the transportation system without depriving the public of adequate protection against unfair treatment.

On the other hand, the public is greatly in need of education. People have too long been led to believe that the interests of the railroads are diametrically opposed to all other business interests; they should be made to understand that the maintenance of the transportation system in an unimpaired state is of vital importance to the economic fabric of the nation, that the railway service should continue to develop and expand, and that existing obstacles to a healthy growth of transportation enterprise should be promptly removed. If suspicion and hostility can be replaced on all sides by a spirit of mutual confidence and tolerance the work of securing needed changes will be easy.

That some adequate system of railroad regulation can be devised which will permit the railroads to prosper and give efficient service at reasonable rates is not to be doubted, and it is with this goal in view that the next steps in railroad regulation must be taken. The United States is not prepared to adopt a program of government ownership of railroads, and it is to be hoped that once the present crisis is passed the railroads will be returned to private management and a system of regulation devised under which satisfactory results may be obtained. We certainly shall never

return to the policy recently abandoned, which has proved such a lamentable failure, and if government ownership is to be avoided we should begin at once to take stock of failures and successes and to make plans for the future. We do not have too much regulation or too little regulation; what we suffer from is an unwholesome combination of good legislation, bad legislation and no legislation. Purposes have been obscured by prejudices; we have been given drastic remedies for imaginary ills and no remedies at all for real diseases. There are a number of radical changes that can be safely made which would go far toward establishing our regulative system on a fundamentally sound basis, and would render easy the working out of the details of a harmonious and constructive policy.

The dual system of regulation as carried on at present inevitably leads to a violation of the fundamental principles upon which regulation is based: that rates shall be just and reasonable, and that they shall not be unduly discriminatory. While it is possible technically to distinguish between interstate and intrastate traffic there is in an economic sense no real distinction between them. If two cents a mile represents a just and reasonable charge for an intrastate passenger journey it can not be possible that a fare of two and a half cents a mile is a just charge for a ride taken under similar conditions but extending across an imaginary line designated as a state boundary. When dissimilar rates exist for two freight services in every way similar except that the haul in one case crosses a state boundary there is no escaping the conclusion that if one of the rates is reasonable the other is not. Whenever a railroad is compelled by virtue of the ruling of a state commission and by the pressure of competition to reduce an interstate rate, supposedly reasonable and declared so by the Interstate Commerce Commission, either the railroad is forced to accept unduly low remuneration or a disagreeable reflection is cast upon the judgment of the federal commission. If an adjustment of the interstate rate is not made to meet changes in an intrastate rate an undue discrimination is created and the dual system becomes the means of defeating the very purpose for which regulation exists. As to how this paradoxical situation may be best treated there is much difference of opinion, some people believing the problem can be met by securing coöperative action of the various regulative agencies, and others inclining to the plan of eliminating state control of railroad rates, leaving

the work entirely to a commission or commissions of the federal government. The fact that nine-tenths of railroad traffic is interstate and consequently already under the jurisdiction of the federal commission would seem to indicate that the remaining tenth could be safely entrusted to its authority without any undue increase of its work and with a considerable gain in the efficiency and uniformity of regulation.

The urgent need for a unified system of regulating the issue of securities by railroad corporations and the almost unanimous belief that this function should be entrusted to federal authority leads one to wonder why it takes so long to secure a law by which this much needed change may be accomplished. When such a law is enacted it is to be hoped that it will also include provision for some supervision of the expenditure of funds derived from the sale of authorized securities. There is a serious question in many minds as to the wisdom with which the large investments placed in the railroad business in recent years have been used. The wholesale expenditure for the construction of huge passenger terminals at a time when the need for improved freight terminal facilities was probably much more pressing has been looked upon with some disfavor both on account of the disparity of income from the freight and passenger business and because in many cases the passenger terminals represent costly duplications of effort with results that do not show much progress toward an ultimate solution of the problem of handling a rapidly congesting passenger traffic.

There should be devised some plan by which needed increases in rates can be secured with more expedition and promptness than appears to be possible under present conditions. It is not advisable that the authority of regulative agencies to suspend proposed increases be withdrawn, but it would probably be helpful if the time of rate suspensions were made shorter than is now customary. It is of the utmost importance that the credit of soundly financed railroads be maintained, and this can be done only if methods are devised for meeting promptly sudden emergencies. Rates are now flexible in but one direction and it is extremely difficult for the carriers to adjust their charges so as to meet the rapid increases in wages and prices of materials. If the power to name minimum as well as maximum rates were given to the Interstate Commerce Commission the income of the railroads would receive a greater

measure of protection. Since the charges which the railroads are allowed to make for their services are strictly regulated by commissions, if there is to be regulation of wages and of prices for materials it should be entrusted to the same authority by which income is controlled.

The adoption of a plan which would insure a more general representation on railroad commissions of the various business interests involved in the success of the railroads would be a step of progress. Laws are passed dealing with the financial management, the accounting, the operation and the rates of railroad corporations, but there is a marked dearth of bankers, engineers, railroad traffic managers, industrial traffic managers and accountants among the appointees to railroad commissions. It is probably too much to expect that under present conditions of government it would be possible to elect executives who would lay aside politics in making appointments to administrative bodies charged with the important duties of regulating private business. The increase of the salaries of commissioners, in order to make the positions attractive to suitably equipped individuals, has usually served only to increase the value of the position as a part of the political spoils and to stimulate the scramble of the unfit for the appointments. The constant change of the personnel of commissions makes it impossible for them to do well the work for which they are chosen. The English custom of providing by law that some members of commissions shall possess certain qualifications might well be given a trial in this country.

And finally as a *sine qua non* of a resumption of private operation provision must be made for the permanency of the operating unity now going into effect. Two things will have to be done. The carriers must be permitted to enter pooling agreements by means of which the financial adjustments necessary to operating unity may be effected; the carriers must be required to combine their physical facilities wherever such combination will result in improved service. There is no reason for limiting the unified "continental railway system" to the duration of the war; its proved advantages will be all the more valuable with the return of peace. It must not be expected that the railroad companies will voluntarily enter agreements for unity of operation, though it is highly probable that the present experience with unification under government

control will render compulsion less difficult. In the main, the joint use of facilities will be confined to terminals, where the wastes of competition have been greatest. Saving must be accomplished, however, through a more elastic system of routing shipments; the expensive duplication in passenger service may be cut down; and the necessity for private car lines and express companies—parasitic organizations which came into existence solely because of the lack of a unified system of operation—will be entirely eliminated; such companies have performed a real public service in the past, but with unity of railroad operation they will exist for no useful purpose. The chief economy will be effected, however, through the reconstruction and reorganization of terminals; it begins to appear that the time is forever past when the shamefully wasteful terminal operation, which exists merely as an evidence of the monopolistic power of a strongly entrenched special privilege, will be permitted to stand unchallenged. The willingness or the unwillingness of the carriers to acquiesce in coöperative arrangements which plainly make for increased efficiency will be the deciding factor in the coming controversy over government ownership.